Q&A: Behind The Brand

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Since the recession, private label products have become more popular than ever, and it looks as though consumers will stick with private label even as the economy recovers. Meanwhile, brand names are taking innovative measures to ensure their products' continued success. *Food Manufacturing* spoke with Ken Sawka, Managing Partner for Outward Insights, about the private label trend and what brand names are doing to keep up.

Q: How has the private label industry evolved into what it is today?

A: Private label products are all about cost savings for the consumer. During economic downturns, private label market shares tend to increase, but once the economy rebounds, private label products tend to give most of that share increase back to branded products. However, in the last 5 years or so, private label products have improved across many facets — product quality, packaging, and so on.

As a result, consumers who purchase private label products today feel less like they are "sacrificing" quality for lower prices. As a result, as the U.S. economy continues its slow recovery from the Great Recession, private label products for the most part have not given back the market share increases that they experienced during the recession.

Q: Since the recession hit, private labels have increasingly become more popular with consumers. How is this impacting brand manufacturers, retailers and their supply chains?

A: Before the recession, brand manufacturers really didn't see private label as a competitive threat. Private label was the "store brand" and didn't merit the attention of the branded manufacturers. Today, that has changed, and brand manufacturers are struggling to understand the competitive challenges private label products present. As private label moves beyond being a "store brand" and acquires unique trade names — such as Great Value, which is one of many Walmart private label "brands" — branded competitors are taking notice.

For retailers, private label products that are perceived by consumers as nearly indistinguishable from national brands serve several purposes. They can increase traffic in the store, as the private label products are only available at individual retailers. They can also allow the retailer to strengthen its own brand image. Again, citing the Walmart example, if consumers perceive Great Value as a quality product, this will reflect well on the Walmart brand.

Q: Often, manufacturers produce brand names as well as private label products. Is this causing somewhat of a conflict of interest for such manufacturers?

A: I don't think so. Most manufacturers successfully separate how they manage branded products from any private label products they might manufacture. And, at the end of the day, they are still selling the products they manufacture to retailers; in the case of private label products, the manufacturer just has an exclusive relationship with the retailer for that product.

Q: Can brand manufacturers and retailers maintain a mutually beneficial relationship?

A: Absolutely. As brand manufacturers reconsider how to deal with the competitive challenge posed by private label, and as retailers understand how to better leverage the benefits of improving private label offerings, the symbiosis in the relationship between manufacturer and retailer is becoming stronger. Unlike in Europe, most categories in the U.S. market are not at the point where private label sales are greater than branded product sales. Nor do large U.S. retailers carry predominantly private label products, like the UK retailer Tesco (though there are a few exceptions, such as Trader Joe's).

Retailers need branded products because consumers want them, and brand manufacturers need private label products because they set a "price floor" that consumers use to determine the value-add of brand products. The challenge is managing that symbiotic relationship to the benefit of both the retailer and the manufacturer.

Q: What should brand manufacturers do in response to this shift toward private labels?

A: Brand manufacturers need to find new ways to innovate and differentiate. For instance, some manufacturers are leveraging new technologies to do so. Kraft foods has developed a kiosk that it may install in grocery stores that uses video analytics to determine, based on facial characteristics, what Kraft products a consumer may find appealing. Coming up with truly differentiating innovations may be one of the biggest challenges facing manufacturers in the next five years.

Q: Will brand manufacturers win over consumers eventually because of the quality of branded products?

A: The quality of their products alone won't be enough. With the improvements in private label quality, manufacturers need to find new points of differentiation. Many food manufacturers, for example, are capitalizing on the health and wellness trend by rushing to make their products healthier by reducing sodium content, adding healthy ingredients and so on. Innovation still seems to be led by national brand manufacturers, with private label products following their lead.

Q: Are there enough benefits for manufacturers to continue to produce brand names?

A: Yes, I believe there are. Large, multi-brand companies like Kraft and Procter & Gamble occupy hundreds of product categories and manage hundreds of brands. These companies continue to derive value from the equity that their brands possess. Brands are valued by consumers and required by retailers, so it's hard to envision a scenario occurring, at least in the next 5–10 years, where manufacturers would begin to question the value of producing branded products.

Q: How are private labels benefiting retailers?

A: Retailers are really seeing their private label products in new ways. Historically, private label products were just a cheaper alternative to brands. However, with the improvements in private label quality and perception, retailers are using private label products to capture more margin, increase store traffic, and reinforce their own retail brands. Some retailers even feel so good about their private label products that when a consumer buys a branded product, the retailer will give away the private label counterpart for free.

Q: How can producing private label products benefit manufacturers?

A: Manufacturers generally use private label manufacturing to manage capacity, allowing them to achieve targeted returns on capital. If volume for a branded product drops, manufacturers often replace that volume by manufacturing private label. Private label manufacturing is a nice hedge against volume volatility and ensures that capital investments in factories and equipment are being adequately utilized.

Q: How much have retailers profited from selling private labels?

A: It's hard to say. Depending on the category, retailers are not necessarily making more profits from private label products, and in some categories private label profits may actually be less than what retailers make from branded product sales. One study I read said that, on average, private label margins are about 10 percent higher than those on similar branded products. I think the real value for retailers comes from using private label products to attract and retain customers, and to contribute to the retailers' brand image.

Q: What do you see in the future for private labels and brand names?

A: I think, in the aftermath of the Great Recession, the relationship between private label and brands has changed — probably irrevocably. If consumers continue to exhibit more frugality and private label products continue to improve their quality, it's feasible that private label will continue to gain share during periods of economic growth, not just during downturns. This will pose a tough challenge to branded products.

I wonder if it's even feasible for the Tesco model to work in the U.S., where retailers sell only private label products. I think this is still a long way off, but it's worth watching. At the end of the day, brand manufacturers' ability to compete against private label will come down to meaningful innovation. Retailers do not yet seem able to match national manufacturers in the quality or pace of product innovation. If brand manufacturers can continually come up with meaningful innovation that improves the perception of their brands in the eyes of the consumers and that benefits retailers at the same time, then brands will continue to play a strong role in U.S. retail.

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